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C O N F I D E N T I A L SECTION 01 OF 03 CARACAS 000844

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E.O. 12958: DECL: 06/12/2018
TAGS: ECON EFIN EAGR PGOV VE
SUBJECT: CORRECTED COPY: CHAVEZ ANNOUNCES NEW ECONOMIC
MEASURES: MUCH ADO, LITTLE SIGNIFICANCE

REF: A. CARACAS 769
¶B. CARACAS 647
¶C. 2007 CARACAS 2130
¶D. CARACAS 313
¶E. CARACAS 494

Classified By: Acting Economic Counselor David Galbraith for reasons 1.
4 (b) and (d).

¶1. (U) This cable is a corrected copy of CARACAS 838, with a pass line to USDA added.

¶2. (C) Summary: President Chavez announced on June 11 a series of economic measures to stimulate domestic production and reduce inflationary pressures. Calling for a national productive alliance, Chavez detailed measures including creation of a USD 1 billion government controlled fund to invest in public-private productive enterprises; support for several other programs to develop mixed and "social production" enterprises; subsidies for small-scale agricultural producers; expedited approval of foreign exchange for businesses who had requests pending for imports of capital goods or raw materials valued at USD 50 thousand or less; the elimination of the tax on financial transactions; and a promise not to cut back on public spending or impose new taxes in 2008. BRV consultations with representatives of key economic sectors supposedly informed the development of these measures, and their announcement was delayed for approximately one week, reportedly partly as a result of sharp disagreements within the BRV. The build-up to the announcement suggests BRV concern that the economy is faltering. The measures, however, are little more than cosmetic and do not address the root causes of Venezuela's economic vulnerability. End summary.

An Awkward Roll-Out

¶3. (SBU) After reports that BRV economic officials were meeting with representatives of key sectors to discuss a series of new economic measures, an announcement was expected during the week of June 2. The Minister of Communication and Information, Andres Izarra, then explained on June 4 that the announcements would be made "in the coming days" once Chavez had designated a new Minister of Finance to replace Rafael Isea, who is Chavez' party's candidate for governor of Aragua. (Note: Chavez has not yet designated a new minister, though press reports suggest he will tap Jose Felix

Ribas, a former Vice-Minister of Planning. End note.) Izarra billed the measures as steps to "reimpulsar", or stimulate, domestic economic production. According to press reports, Planning Minister Haiman El Troudi added that the measures amounted to an "accord" with different economic actors to reduce inflationary pressures. A local economist told Econoff that, according to a well-placed contact of his, the apparent delay in announcing the measures resulted from sharp disagreements between pragmatists and ideologues within the BRV and its interest groups.

¶4. (SBU) The June 11 announcement took place in a context of increasing concern about the Venezuelan economy. Central Bank (BCV) figures released in May showed that economic growth declined significantly in the first quarter of 2008 relative to the first quarter of 2007 (ref A). On June 9, the BCV released inflation figures according to which May had the highest inflation of any month to date in 2008 (3.2 percent nationwide) and annual inflation in Caracas rose above 30 percent (May 2007 to May 2008). Chavez made the announcement at prime-time in cadena (obligating all local channels to carry it) in a large conference room filled with ministers, party loyalists, and a large number of business people including the presidents of Polar (Venezuela's largest food processing company) and two major banks.

The Measures

¶5. (SBU) Chavez began his almost three-hour speech with an attack on capitalism, arguing that the U.S. economy was in crisis while the Venezuelan economy was attracting

investment. Claiming that socialism does not exclude the private sector, he went on to call for a national "productive alliance" that included the private sector. He then turned to specific measures designed to improve national production. The first series of measures revolved around the use of state funds to support mixed or socialist enterprises. For example, he announced a USD 1 billion fund overseen by the BRV to make soft loans to mixed enterprises in strategic areas of production and the creation of programs "Fabrica Adentro II and III" to fund state and mixed enterprises. Chavez also announced a series of subsidies for agricultural producers, including guaranteed minimum prices for sunflower and soybeans, subsidies for other products based on production costs, and debt relief for small farmers with outstanding loans from the state entity Fondafa. (Note: The modalities of many of these announced programs are unclear. End note.)

¶6. (SBU) Turning to macroeconomic issues, Chavez announced a plan to reduce bureaucracy at CADIVI, the BRV commission that regulates foreign exchange, whereby businesses that had existing requests to import capital goods or raw materials valued at USD 50,000 or less would receive authorization from CADIVI for such requests for the rest of the year without having to submit previously required paperwork (ref B). (Note: The president of CADIVI said on June 12 that it would take one month for this measure to be implemented. End note.) Chavez said that the 1.5 percent tax on many financial transactions (ITF; ref C) would be eliminated, noting that it was regressive and had inflationary consequences, and promised there would be no new taxes for the rest of the year. Finally, however, Chavez noted that he had no intention of cutting back on spending in the face of inflationary concerns and read a laundry list of projects under way.

The Private Sector Response

¶7. (SBU) The private sector response has been mixed. The

presidents of Fedecamaras and Consecomercio, two of the largest industry organizations and consistent critics of BRV economic policies, said that they expected the new measures to fail, as past BRV measures had. In a June 12 meeting, members of VenAmCham's economic committee agreed that the measures represented a change in tactics but not strategy; that they were mostly very imprecise; and that, with the exception of the elimination of the ITF, they would have little impact on major business enterprises. A contact in the agriculture sector predicted the measures would have little impact on agricultural production or food processing. The presidents of Empreven and Fedeindustria, two business organizations with close ties to the BRV, were, predictably, much more positive, arguing that the measures met important demands of the productive sector and would stimulate production. Two presidents of major banks present at the speech also expressed satisfaction with the content to the press. (Note: Banks were strongly opposed to the ITF, so its elimination will be a relief to them. End note.)

Comment

¶8. (C) The measures announced by Chavez are superficial at best and are unlikely to reduce inflation or increase production significantly. The elimination of the ITF should be reflected in lower inflation in the coming two months (relative to what it would otherwise have been), just as its imposition likely resulted in higher inflation late last year. A far more important driver of inflation, however, has been fiscal spending (ref D). Chavez' assurance that the BRV would not cut spending to reduce inflationary pressures suggests that the BRV will be injecting more money into the economy in the run-up to state and local elections later this year.

¶9. (C) On the production side, the new measures will do little to overcome business people's reluctance to invest, given continued nationalizations and other threats to private property rights (ref E). Changing the rationing priorities

and/or the bureaucratic processes associated with CADIVI does not change the fundamental problems that result from having an overvalued currency and foreign exchange controls, namely that the government has to play the role of central planner and that opportunities for corruption abound (ref B). Chavez did not, however, make any changes in the exchange rate itself. The agricultural subsidies seem to be mainly directed at smaller producers, whose output represents only a small share of overall production. Finally, many of the measures seem to give the BRV an even greater opportunity to distribute economic largesse on a discretionary basis, a fact which perhaps explains the enthusiasm shown by business associations close to the BRV and which should not be surprising in an election year. End comment.
Downes